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Southwestern Bell

July 19, 1994

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Stephen S. Melnikoff
Vice President
Federal Regulatory

Ex Parte

Mr. William F. Caton
Acting Secretary
Federal Communications Commission
1919 M Street, N.W., Room 222
Washington, D.C. 20554

Re: MFS Petition for Rulemaking (RM-8480)

Dear Mr. Caton:

In accordance with Commission rules governing ex parte presentations, please be advised that on Friday, July 15, Paul Cooper, Division Manager-External Affairs and Tim Morrissey, Area Manager-External Affairs and the undersigned representing Southwestern Bell met with Suzanne Tetreault and Mark Nadel of the Policy and Program Planning Division and Larry Povich of the Industry Analysis Division regarding issues associated with the above reference proceeding. Southwestern Bell's positions on such issues are of public record. Attached is material provided in the meeting. Some of the material provided in the meeting will be filed at a later date as it is presently in the process of being reproduced.

Due to the fact that the meeting was held late in the day, this letter is being filed on the next business day. If you have any questions, please let me know.

Sincerely,

Attachment

cc: Suzanne Tetreault
Mark Nadel
Larry Povich

No. of Copies rec'd 0+1
List A B C D E

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UNIVERSAL SERVICE

CURRENT FEDERAL ISSUES AND THEIR POTENTIAL IMPACT ON TELEPHONE COMPANIES AND THEIR CUSTOMERS

SOUTHWESTERN BELL TELEPHONE COMPANY (SWBT)

IMPLICIT SUPPORT MECHANISMS

WHY ARE WE DISCUSSING?

Due to the Introduction of Additional Competition and The Resulting Need For Access Restructure:

- Need to Price at Market Rate

- Support for existing Universal Service/High Cost at stake and may be lost without changes. Current implicit support results in:

  - Affordable Local Exchange Service

  - Affordable Geographic Service

QUESTIONS RAISED

1. **What Is Universal Service?**

2. **How do we currently provide Universal Service?**

3. **How Large is Universal Service Support?**

   - Why is support at this level?

4. **Options for Maintenance of Universal Service Support**

5. **Proposal for Maintenance of Support in a Competitive Environment**

   - Rate Rebalancing
   - Targeted Customer Support
   - Committment to Carrier of Last Resort Obligations

6. **Effect of the Broadband Network**

SWBT'S
UNIVERSAL SERVICE DEFINITION

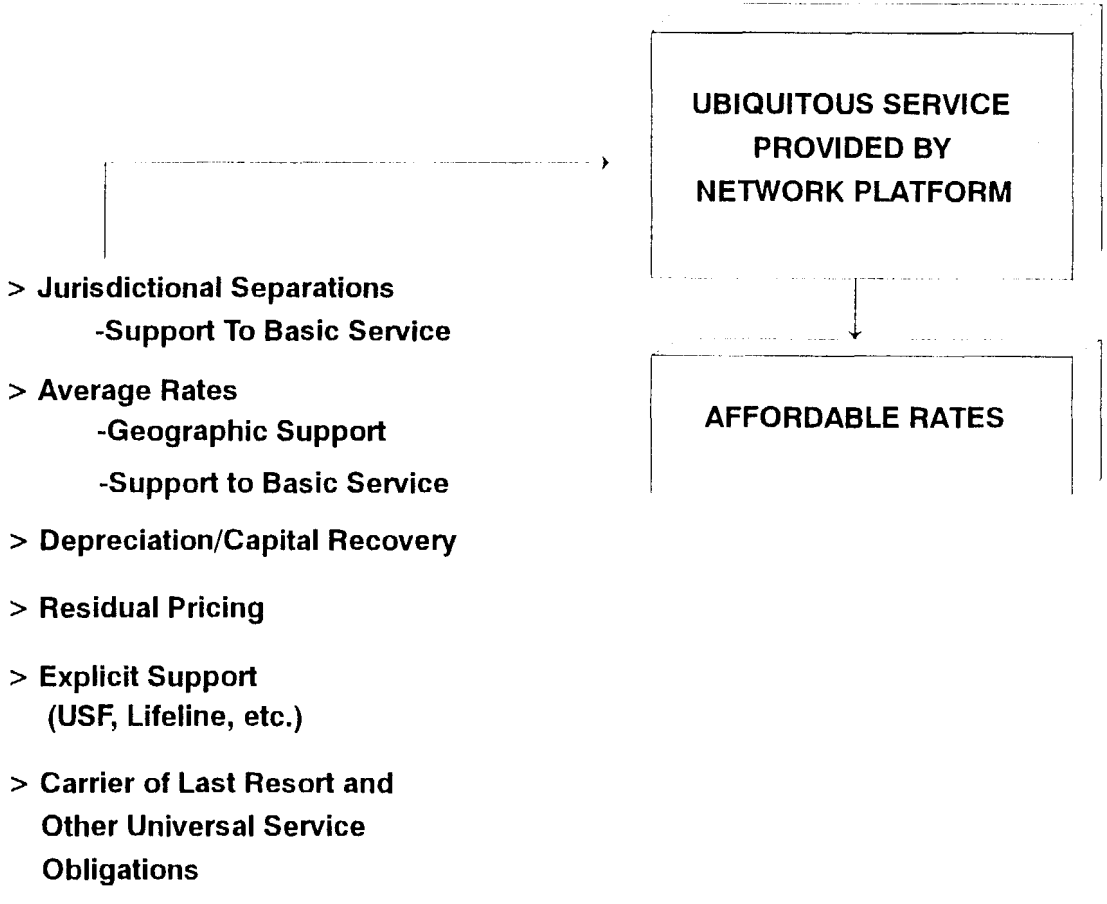
Universal Service is the conceptual goal of making telephone service widely available throughout the United States at reasonable rates. In practice it is:

- Use of a universally available network (loops, trunks, switches) by all geographic areas (low cost, high cost, etc.)

- Reasonable rates for two-way switched voice service over that network in all geographic areas (low cost, high cost, etc.)

EXISTING UNIVERSAL SERVICE SUPPORT

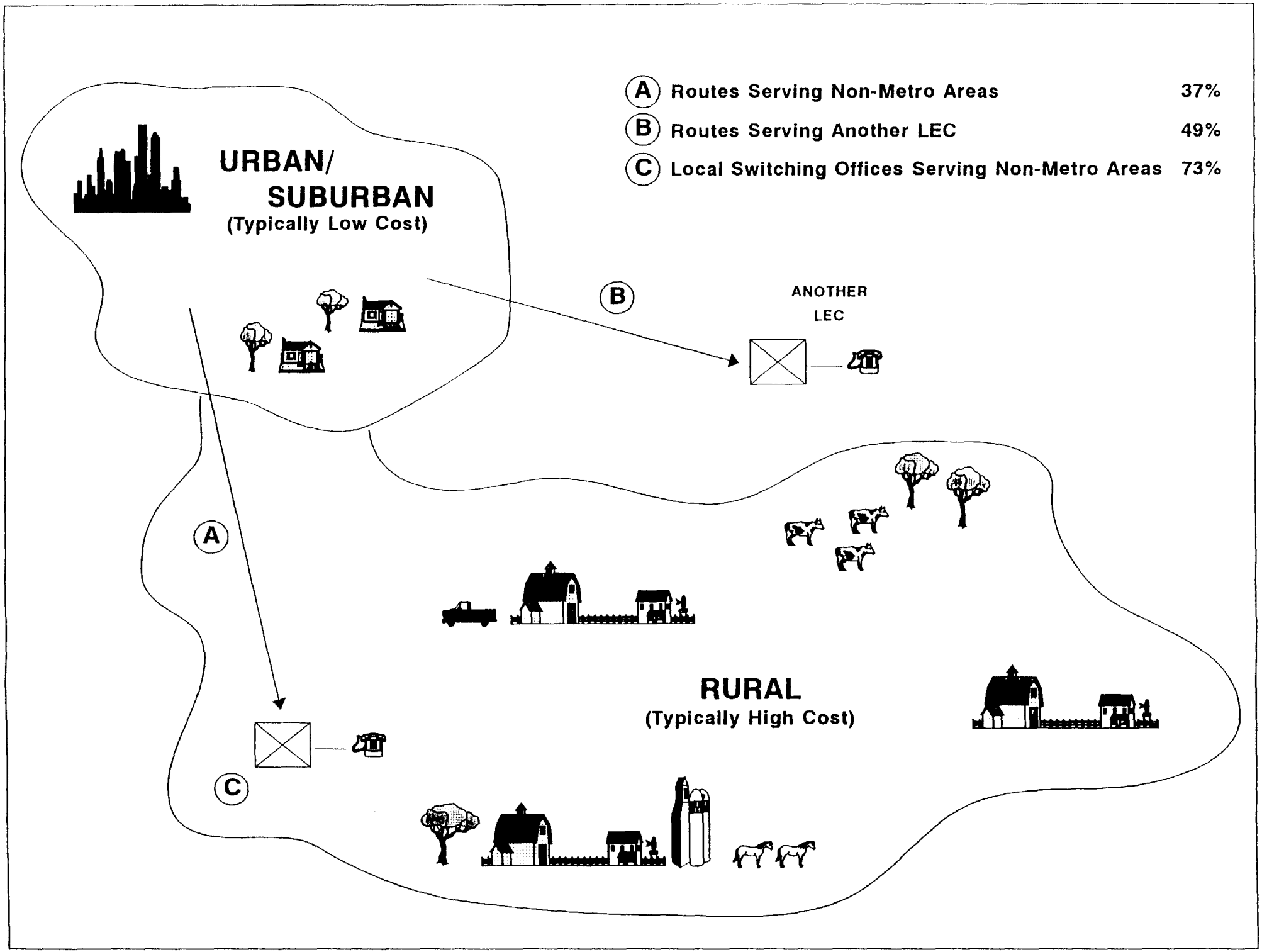
WITH MINIMAL COMPETITION



ESTIMATED AMOUNT OF CURRENT IMPLICIT CONTRIBUTION / SUPPORT
TOLL & ACCESS SERVICES

(Est. $ in Millions 000,000)

Description	Nationwide		SWBT	
	Interstate	Intrastate	Interstate	Intrastate
AVERAGE PRICING-Transport	$6,500M	$3,800M	$210M	$140M
AVERAGE PRICING-Loc Sw			$170M	$130M
Carrier Common Line (CCL)			$310M	$460M
AVERAGE PRICING-State Toll	N/A	$8,300M	N/A	$640M
TOTAL - SUPPORT IN RATES	$6,500M	$12,100M	$690M	$1,370M
	MONSON-ROLFS STUDY			
CONTRIBUTION / SUPPORT	$18,600M		$2,060M	


A Routes Serving Non-Metro Areas 37%
B Routes Serving Another LEC 49%
C Local Switching Offices Serving Non-Metro Areas 73%
URBAN/
SUBURBAN
(Typically Low Cost)
B
ANOTHER
LEC
A
C
RURAL
(Typically High Cost)

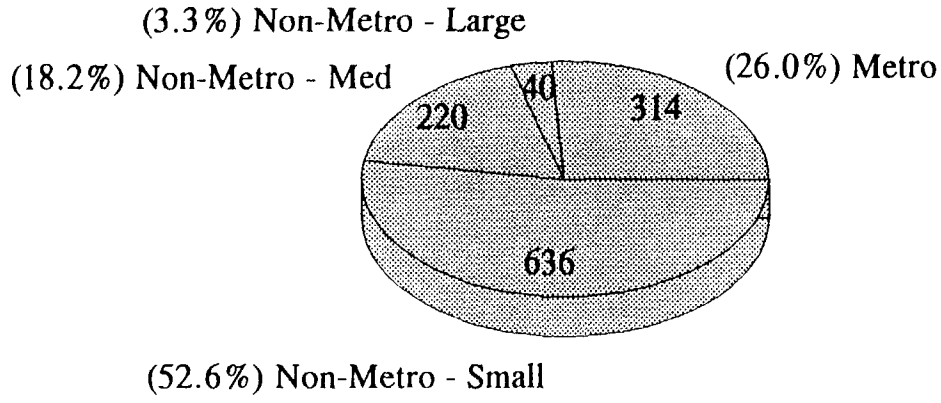
STUDY IN PROGRESS

Analyses of:

1. Cost and Revenue Distribution by Groupings of Wire Centers

2. Demographics and Penetration

SWBT Number of Wire Centers

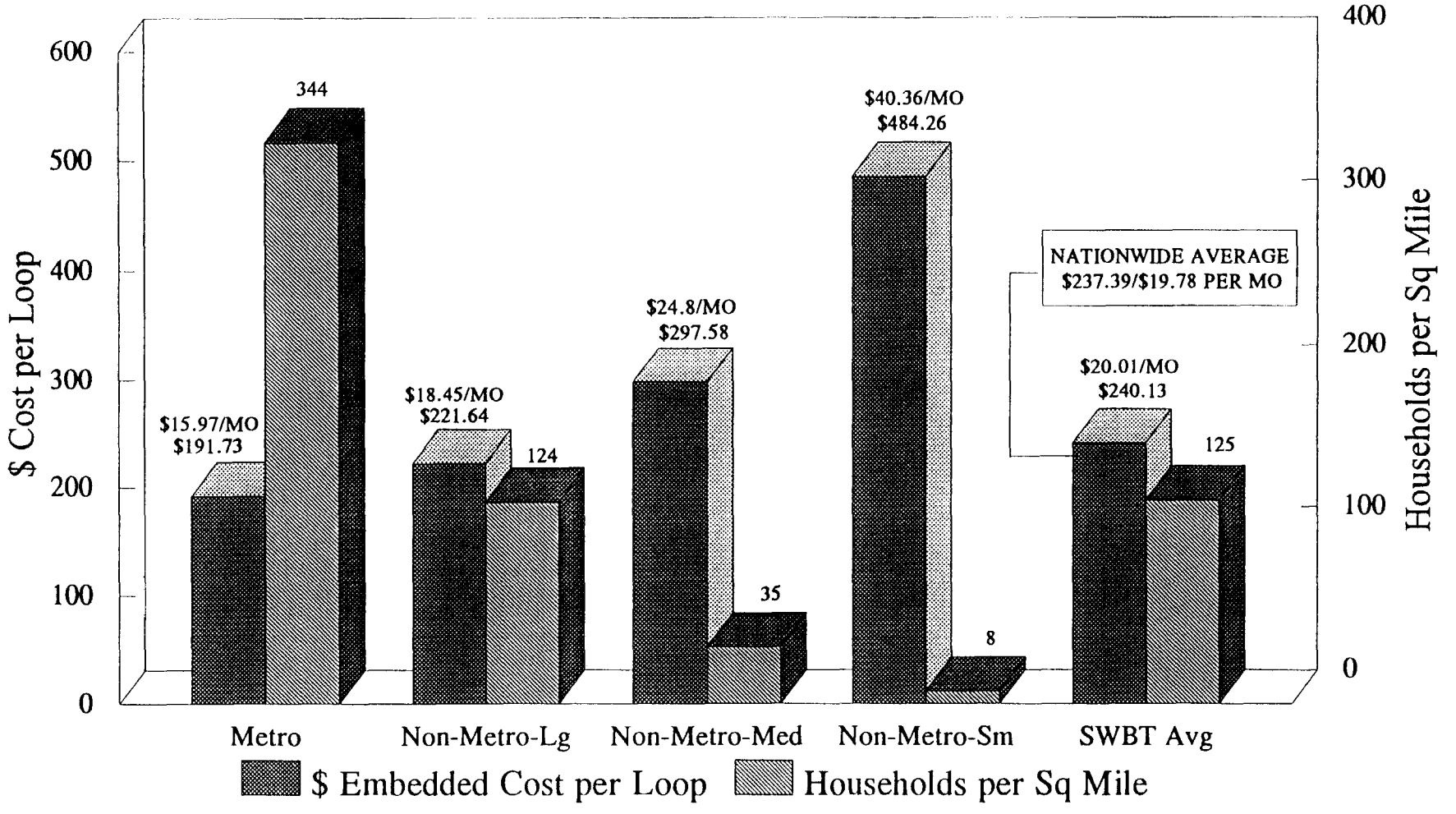


Represents 97 percent of SWBT end offices in service during 1993

Metro - SWBT 12 Major Metros
Non-Metro Large - Over 25,000 lines
Non-Metro Medium - 5,000 to 25,000 lines
Non-Metro Small - Under 5,000 lines

SWBT'S TERRITORY IS MADE UP OF A MIX OF WIRE CENTERS WITH A SUBSTANTIAL NUMBER OF THEM BEING LOCATED IN SMALL NON-METRO AREAS.

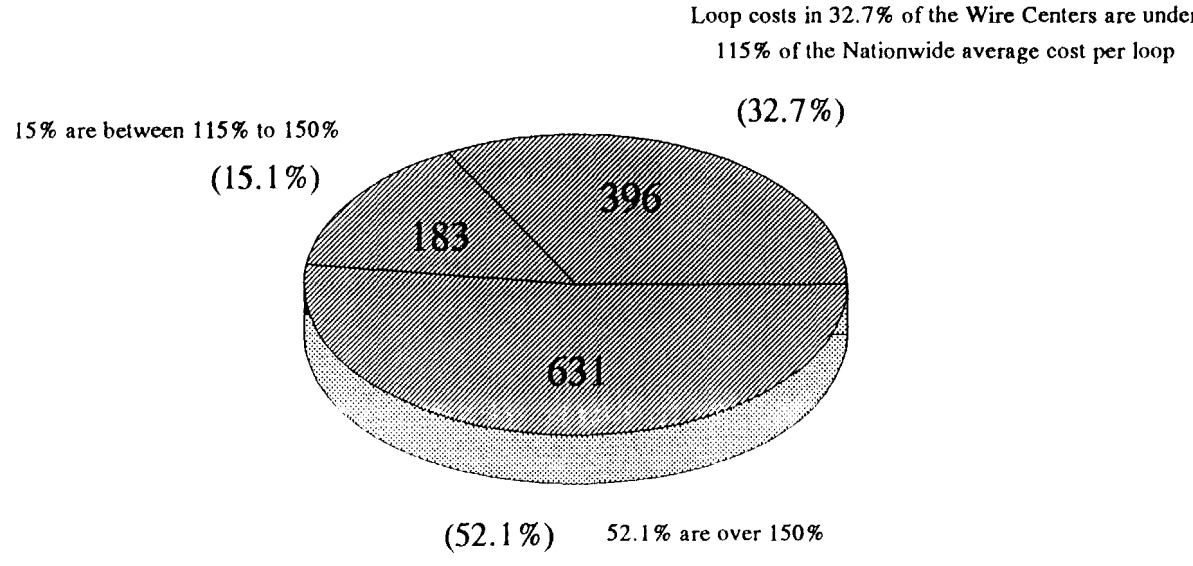
SWBT Total Loop Cost per Loop and Household Density



Based on embedded loop cost derived using USF Loop Cost rules as defined in FCC PT 36.

THERE IS A SIGNIFICANT CORRELATION BETWEEN LOOP COSTS AND DENSITY. LOOP COST FOR HIGH DENSITY AREAS ARE LOWER AND LOOP COST FOR LOWER DENSITY AREAS ARE MUGH HIGHER. SWBT SERVES A SIGNIFICANT NUMBER OF LOW DENSITY AREAS.

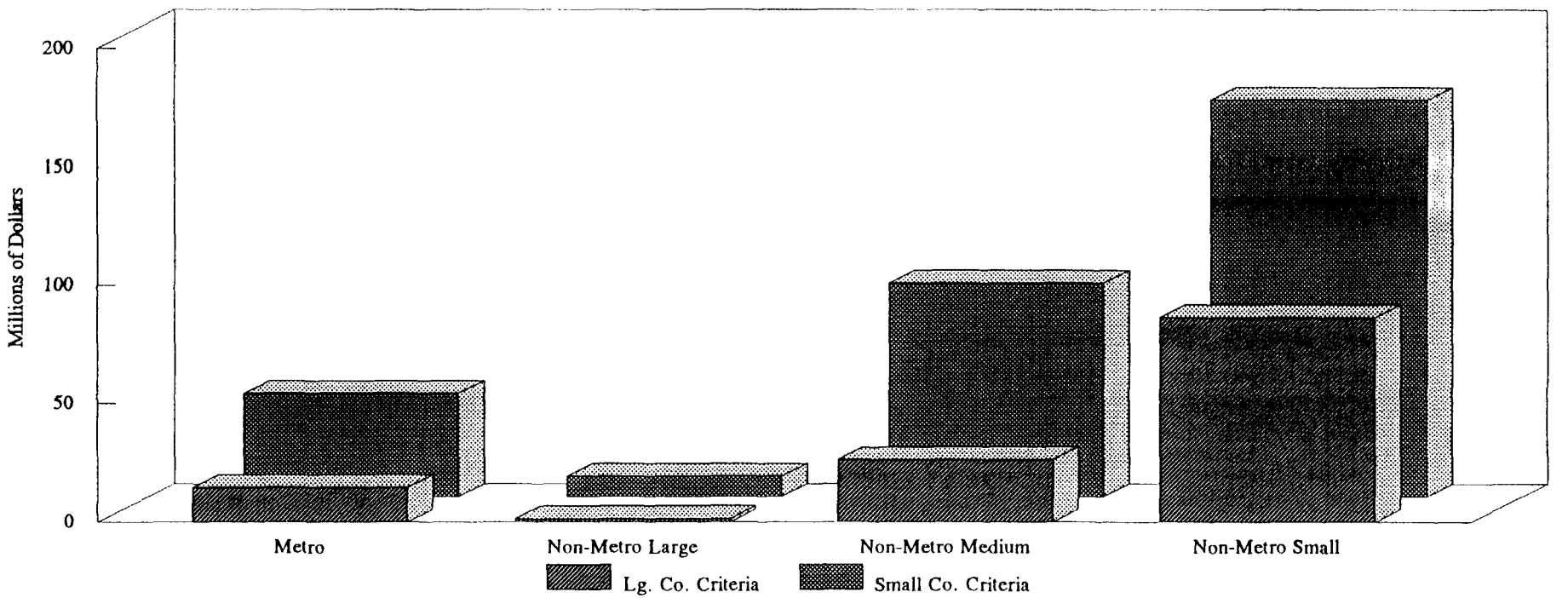
SWBT Total Loop Cost Analyzed by Wire Center by USF Criteria



Category percentages represent percentage relationship of SWBT wire center loop cost to nationwide average loop cost.

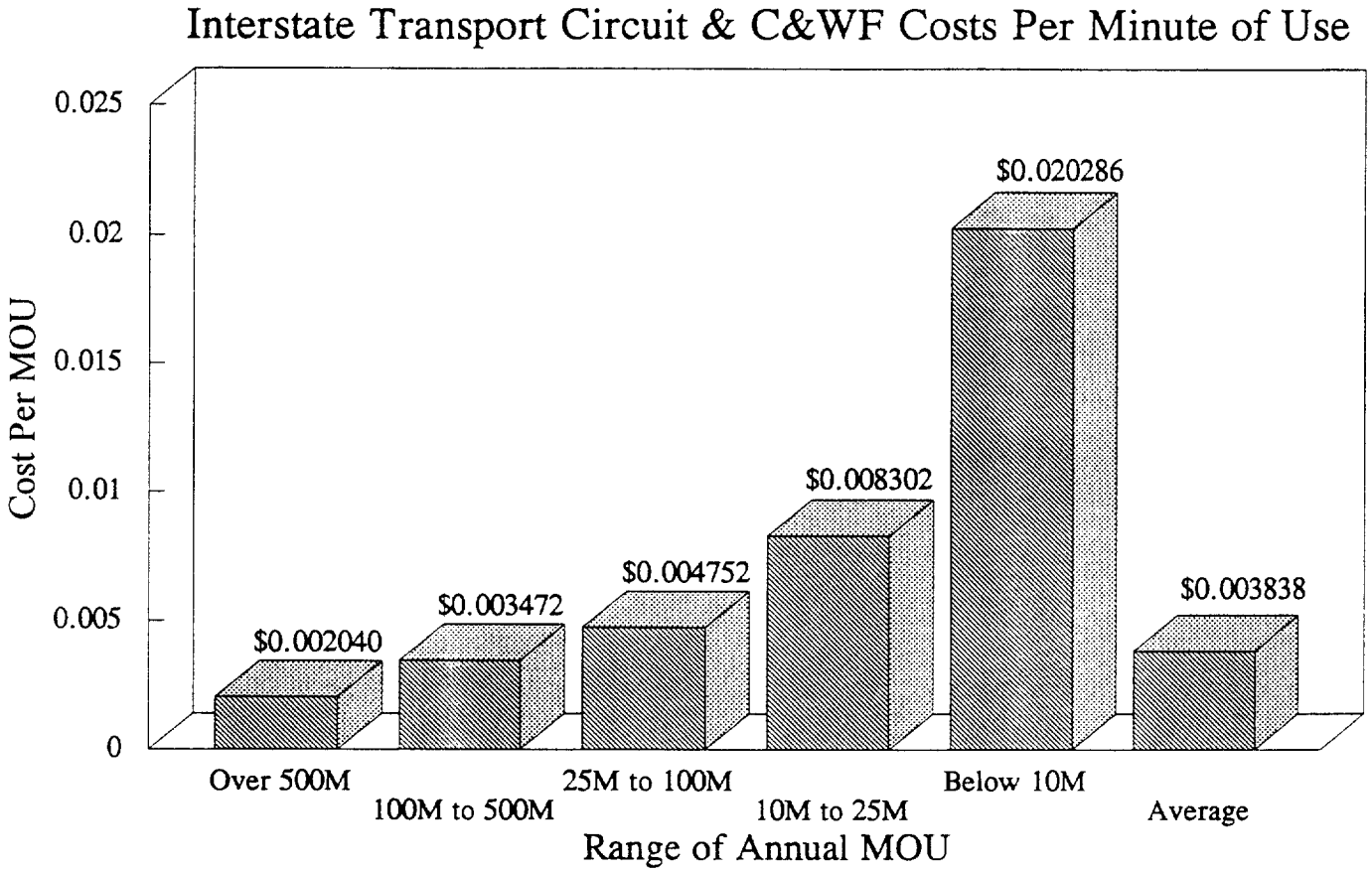
LOOP COST FOR A SIGNIFICANT NUMBER OF SWBT WIRE CENTERS EXCEED NATIONWIDE AVERAGE COST.

SWBT Hypothetical USF Support



	Metro	Non-Metro Lg.	Non-Metro Med.	Non-Metro Small	Total
Lg. Co. Support	$15	$2	$26	$87	$130
Small Co. Support	$44	$9	$90	$168	$311
Total Loop Rev. Req.	$1,467	$319	$703	$518	$3,007

IF USF SUPPORT CRITERIA WERE APPLIED TO SWBT WIRE CENTERS, SWBT MAY QUALIFY FOR UP TO $311M OF SUPPORT. THIS AND OTHER CCL SUPPORT IS INCLUDED IN SWBT'S CURRENT RATES.



Reprents 1992 annual cost data

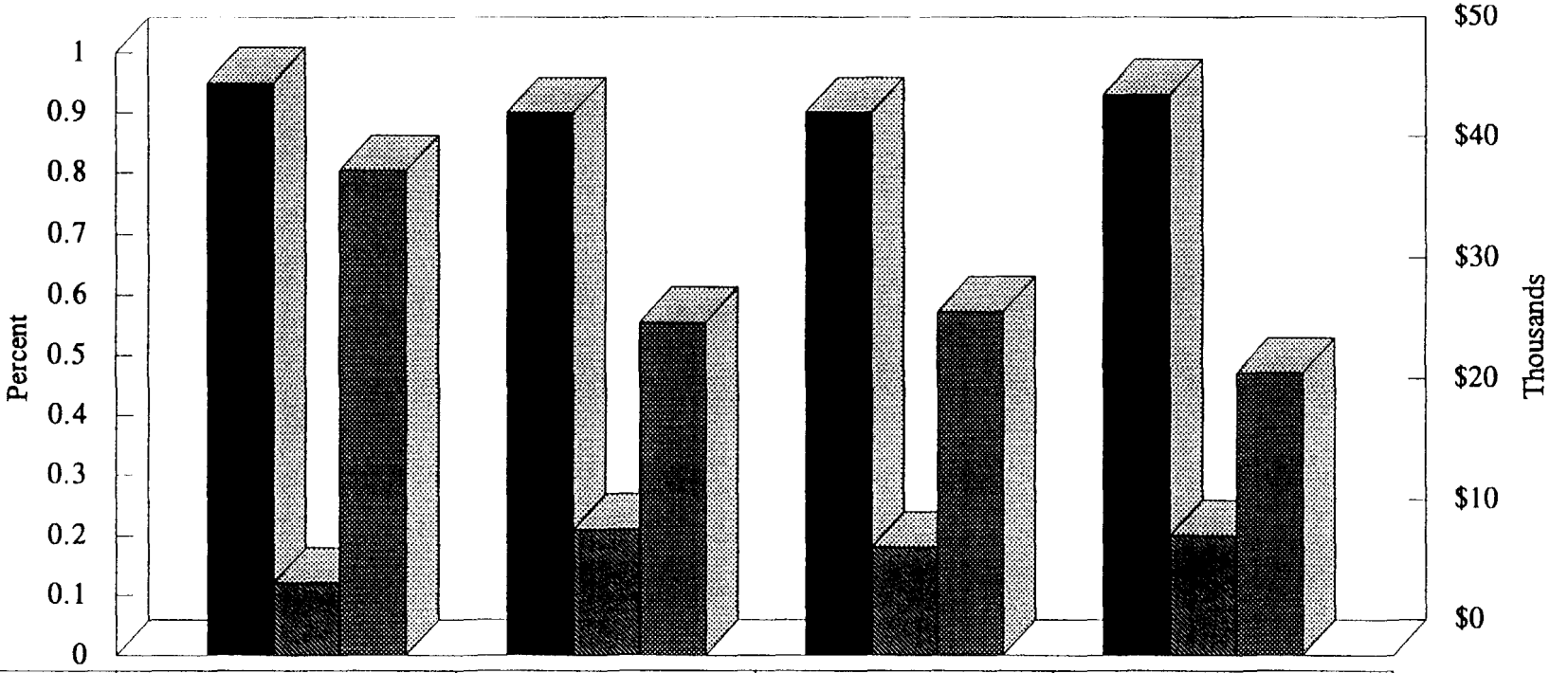
Annual Minutes	Wire Centers		Avg. Access Lines		INTERSTATE TRANSPORT				
	Metro	Non-Metro	Metro	Non-Metro	Circuits	MOU (Millions)	MOU Per Circuit/Mo.	Rev Req** ($ Millions)	(l) Revenue Rqrmnt/MOU
Over 500M	20	3	52,515	34,318	197,561	28,342	11,955	58	0.002040
100M to 500M	55	39	49,920	31,161	189,424	16,920	7,443	59	0.003472
25M to 100M	126	85	25,807	15,794	155,041	11,012	5,919	52	0.004752
10M to 25M	57	133	10,341	7,787	56,098	3,167	4,705	26	0.008302
Below 10M	82	673	2,313	1,751	76,857	2,004	2,172	41	0.020286
Total/Average	340	933	23,020	5,225	674,981	61,444	7,586	236	0.003838

* Includes tandem offices.

** Excludes tandem switching, Category 2, related costs and GSF cost shift.

THE TRANSPORT COSTS ASSOCIATED WITH SWBT'S LOW VOLUME WIRE CENTERS ARE SUBSTANTIALLY GREATER THAN THE AVERAGE COST AND THE HIGH VOLUME WIRE CENTER COSTS ARE LESS THAN THE AVERAGE COST. THIS HAS CAUSED A SIGNIFICANT PORTION OF THE $214 MILLION FEDERAL INTERCONNECTION CHARGE.

Customer Demographics



	Metro	Non-Metro Lg.	Non-Metro Med.	Non-Metro Small
% Cust Penetration	95%	90%	90%	93%
% Cust below Pvty	12%	21%	18%	20%
Avg. HH Inc.	$40,181	$27,656	$28,554	$23,457

Number of Customers below poverty: Metro-568,680; Non-Metros: Large-194,252, Medium - 314,689, and Small - 182,713.

Source: 1990 Census block data assigned to SWBT wire centers.

OPTIONS FOR FUNDING PROVISION/MAINTENANCE OF UNIVERSAL SERVICE SUPPORT

RATE REBALANCING

+

EXISTING EXPLICIT SUPPORT

+

TARGETED CUSTOMER SUPPORT (WHERE NECESSARY)

JURISDICTIONAL SHIFTS

LITTLE RATE REBALANCING

+

TARGETED EXISTING EXPLICIT SUPPORT

+

SUBSTANTIAL ADDITIONAL LEC SUPPORT FUND TO MAINTAIN UNIVERSAL SERVICE

+

TARGETED CUSTOMER SUPPORT (WHERE NECESSARY)

POSSIBILITIES:

> Maintain and Possibly Deaverage Interconnection Charge (IC) For Transport

> Extend IC to CCL, Local Switching

> New Rate Elements

> SLC Increases

> Deaveraging - Geographic
- Res/Bus for Access

> Likely Not the Answer-
Proper Pricing Is the Answer

> Possible Changes:

		IS Effect
NTS	20% < 25% > 30%	(1.7B) to 1.7B
Mktg		(200M) to 30M
Loc Sw		230M

> Protracted Proceedings - Each Competitor Seeking Self Serving Advantage

> Universal Service May be at Risk - New Fund: Sustainability?

> Promotes Cost Based Rate of Return Regulation

PROPOSED UNIVERSAL SERVICE SUPPORT

WITH MINIMAL COMPETITION

> Jurisdictional Separations
>
> -Support To Basic Service

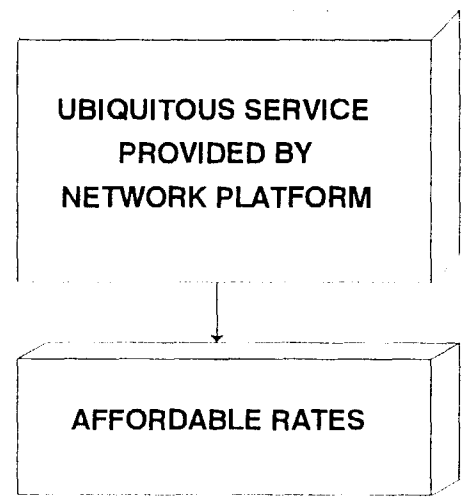
> Average Rates
>
> -Geographic Support
>
> -Support to Basic Service

> Depreciation/Capital Recovery

> Residual Pricing

> Explicit Support
> (USF, Lifeline, etc.)

> Carrier of Last Resort and
> Other Universal Service
> Obligations



WITH FURTHER COMPETITION

> Retain Explicit Support

> Deal With Implicit Support
> Via Rate Rebalancing

> Rate Rebalancing Minimizes
> Further Explicit Support

> Target Additional Explicit
> Support to Customers on
> a Needs Tested Basis

> Will Continue Carrier of Last
> Resort Obligations and
> Other Universal Service
> Obligations Given Recovery

ADVANTAGES OF PRICING APPROACH

ALLOWS COMPETITION AND LESS REGULATION.

- Current average pricing may incent uneconomic competition in high volume areas and may discourage it in low volume higher cost areas.

MINIMIZES FURTHER EXPLICIT SUPPORT PAYMENTS FROM ALL MARKET PLAYERS THROUGH PRICING FLEXIBILITY.

- Continue current industry explicit support (USF, Lifeline, Linkup, TRS, LTS) of approximately $1B.

AFTER RATE RESTRUCTURE, TARGETS EXPLICIT SUPPORT TO CUSTOMERS BASED ON NEEDS TEST.

ALLOWS INDIVIDUAL JURISDICTIONS TO MOVE AT THEIR OWN PACE IN RESTRUCTURING THE RECOVERY OF SUPPORT.

ENCOURAGES THE DEVELOPMENT OF NEW LOW COST TECHNOLOGIES TO SERVE LOWER VOLUME, HIGHER COST AREAS IN ORDER TO REDUCE RATES.

UNIVERSAL PROVISION OF BROADBAND SERVICES AND NEW TECHNOLOGIES

ISSUES

- Major Expansion of Universal Service Costs/Support
- Allocation/Recovery of New Services/Technologies
  - Which Jurisdiction - Who Pays?
  - Cost/Revenue Mismatch?
- Cost of Broadband Network could approach $85/loop per month

PARTING THOUGHTS

1. Rate Rebalancing with the introduction of competition is not a new concept.

   Two major Federal examples are:

   - With deregulation of CPE, approximately $1 billion of interstate support was phased out of the Federal jurisdiction and transferred to intrastate for recovery.

   - With the introduction of long distance competition:

     - Approximately $3.5 billion in interstate loop support was removed from IXC access rates and charged to end users.

     - Approximately $1 billion in interstate local switching support was transferred to intrastate for recovery.

TOTAL - AT LEAST $5.5 BILLION IN ONLY FEDERAL RATE REBALANCING

2. With the introduction of further competition, significant levels of remaining interstate and intrastate support must be dealt with. The best and simplest way is through Rate Rebalancing.

EXPLICIT SUPPORT MECHANISMS

SUMMARY EXPLICIT INTERSTATE SUPPORT

SUBSIDY	*PAID TO*	*FUNDED BY*	*BILLED BY*	*SUPPORT LEVEL*
USF	LECs with high unseparated loop costs - (above 115% Nationwide avg.)	IXCs serving > .05% of Presubscribed Lines	NECA on Presubscribed Lines	$725M
LTS	NECA CCL Tariff participants	IXCs	LECs out of the CL pool additive to the CCL rate	$323M
DEM	Qualifying LECs	Qualifying LEC Access Rates	Qualifying LEC Access Rates	$259M
Lifeline	LECs; Reduces or eliminates SLC Charges for low income subscribers	IXCs serving > .05% of end Users	NECA On Presubscribed Lines	$150M
Linkup	LECs; Reduces installation charges for low Income subscribers			$15M
TRS	TRS service provider	All IS service providers based on their share of IS revenues	NECA based on IS revenue share	$30M

EXPLICIT SUPPORT - THE UNIVERSAL SERVICE FUND (USF)

ISSUES

- GROWTH OF THE FUND
- TARGETING OF THE FUND/NEED
  - RETARGETED TO LOW VOLUME, HIGH COST EXCHANGES
- ALLOCATION OF USF RECOVERY
- CLASSIFICATION OF COST

EXPLICIT SUPPORT - DIAL EQUIPMENT MINUTES (DEM) WEIGHTING

ISSUES

- APPROPRIATENESS/TARGETING
- RATE DISPARITY CAUSED BY THE WEIGHTING AND ITS RECOVERY
- BULK BILL
- EFFECT ON INTRASTATE MIRRORING